COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

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BLACKSTONE GAS COMPANY	)	**D.T.E. 01-50**
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INITIAL BRIEF

OF

BLACKSTONE GAS COMPANY

October 1, 2001

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I. INTRODUCTION

Blackstone Gas Company ("Blackstone" or the "Company") is a very small investor-owned utility with total annual revenues of approximately $ 1.1 million which includes $483,193 of CGA revenues during the test year. Exh. AG-1-2 (Annual Return for 2000). Blackstone distributes and sells gas at retail to 1031 customers, 923 of which are residential customers and 108 are commercial in the towns of Blackstone and Bellingham. The Company has less than ten full and part-time employees that perform all the day to day operations and recordkeeping of a distribution utility. These statistics demonstrate that the Company does not have the financial or human resources to provide the Department of Telecommunications and Energy ("Department") with costly cost of capital or wage studies or other reports in the same detail and sophistication of some of the other larger distribution companies. To require such studies will require the addition of several employees or consultants at a significant additional cost to ratepayers. The Company in this filing has attempted to provide the necessary information and detail within its current resources. The Company cannot be held to the same standard of detail as these larger companies. A denial of the requested rate increase will not allow the Company to provide additional information, but less.

A. Statement of the Case

Blackstone agrees with the statement of the case as provided by the Attorney General in its Initial Brief with one significant addition. The Attorney General presented no witness or affirmative evidence in this case or statement of issues.

B. Due Process

Several arguments raised by the Attorney General in its Initial Brief were never raised during the proceedings by the Attorney General. Thus, Blackstone has had insufficient notice that certain of its costs or expenses were at issue and has been denied reasonable opportunity to present evidence as required by the Administrative procedure Act, G.L. c. 30A, §§ 10, 11. Additional information is available in various filings by Blackstone with the Department including recent cost of gas adjustment filings, Load and Supply Forecast and gas supply contract cases in DTE 00-71 and DTE 00-81. Blackstone requests that its last three annual cost gas adjustment filings be incorporated by reference in this proceeding as well as dockets DTE 00-71 and DTE 00-81. Moreover, Blackstone presents a Motion to Supplement the Record with an Affidavit of James Wojcik.

II. REVENUE REQUIREMENT

A. Customer Billing Units

The Attorney General wrongly suggests that the billings of Blackstone to its customers during the past four years has been inaccurate. AG. Br. 4. This claim is made based on Citygate Sendout and Billings to customers as reported by the Company in Annual Returns to the Department, Exh. AG-1-2. Blackstone does not disagree that during the last four years billing units to customers have exceeded purchased gas units. However, the Attorney General has provided no credible evidence that the error is the result of a problem with Blackstone Gas customer metering or billing. The Blackstone meters are calibrated by Bay State Gas Company and there is no evidence of any inaccuracy. Tr. 1-68.

The problem was described by the Company's witness Ms. Smith as a metering problem of the interstate pipeline company. Tr. 1-64,65; Exh. DTE-1-29. Blackstone is one of the smallest customers of Tennessee Gas Pipeline Company and any metering problem with Blackstone purchases amounts to a rounding error for Tennessee. Moreover, Ms. Smith indicated that "in terms of what customers have been billing, we have been working for this Company for, I think, ten years, and we have observed what customers use in particular weather, and in terms of customer sales, nothing abnormal has happened." Tr. 1-66. In addition, Department records from the Consumer Division over the last three years, which Blackstone requests be incorporated by reference, do not contain a single customer complaint regarding a metering or billing problem. In the past year, as testified to by Ms. Smith and as illustrated in the September 2001 CGA filing of the Company, the metering problem has gone in the other direction, as the bill quantities of gas have been much larger than gas sales. According to the Attorney General's reasoning, Blackstone for the last year must have been underbilling its customers. As noted by Ms. Smith, in previous years metering errors have accrued to the benefit of Blackstone's customers, as the dollars savings from not being billed for all gas used have been passed back to customers through the CGA reconciliation.

The suggestion by the Attorney General that there is no metering error even though the record supports the existence of a metering error, and that Blackstone rather has overbilled its customers, is totally unwarranted.

Blackstone has kept the Gas Division of the Department advised of recurrent billing problems with Tennessee. If the Attorney General had wanted any more detail he could have asked for it. The Department should reject the suggestion by the Attorney General that the Company's proposed rate increase should be rejected until the Company explains all discrepancies.

B. Cost of Capital

The Company submitted a revised cost of capital analysis in RR-DTE-4. This response also made two corrections to reduce the rate base for customer contributions and the reserve for deferred income taxes. In Worksheet 3 the Company calculated a normalized cost of capital equal to the proposed rate base of the Company of $1,361,658. The average weighted cost of capital of 9.72% in Worksheet 3 should be utilized as the cost of capital for this case. This computation is consistent with that request by the Department and that described as appropriate by the Attorney General. This calculation treats as equity only proprietary capital, and all other financing, including additional long-term financing, as debt. See also Blackstone Exhibit 4.

C. Rate Base

1. Post-Test Year Additions

The Company proposed three adjustments to its rate base for post-test year plant additions. The plant additions include (1) transportation equipment, (2) computer software, and (3) tools and other shop equipment. In preparing the response to RR-DTE-4, the

Company discovered that customer contributions and the reserve for deferred taxes had been added into rate base, rather than used to reduce rate base, as appropriate. The Company, on its own initiative, made these adjustments to reduce the requested rate base to $1,361,658, which includes the three pro forma adjustments.

The Department's precedent regarding a company's post-test year additions to rate base is evidenced in the Orders in Nantucket Electric Company, D.P.U. 91-106/138, pp. 90-91 and Assabet Water Company, D.P.U. 95-92, p. 6. "With respect to plant installed after the end of the test year, it is the Department's policy not to adjust year-end rate base, unless the utility demonstrates that the addition represents a significant investment which has a substantial impact on a company's rate base." Id.

The addition of the transportation equipment by the Company, meets this test. The new transportation equipment replaces two 1977 trucks that had been in service for over twenty years. The new equipment includes an International (dump) Truck with a cost of $61,469 and a second truck, a Chevrolet Express with a cost of $29,249. Exhs. AG-2-15 and AG-2-15 Supplemental. The total purchase price for these two trucks added to rate base in the revised cost of service, Exh. Blackstone-4, is $90,709.[1] These two trucks amount to a significant addition for the Company which has a total rate base prior to the pro forma adjustments of $1,251,249. Id. These two trucks amount to a 7.25% addition to rate base.

[1] The correct number is $90,718.

The Attorney General tries to minimize the impact on rate base of the transportation additions by calculating a percentage increase for each truck. The Attorney General's calculations are incorrect as he includes the pro forma adjustments in the rate base to calculate each separate pro forma adjustment. The correct calculation for the trucks individually is 4.91% for the International truck and 2.34% for the Chevrolet Express.

The Company should not be penalized for its frugality in not replacing two trucks for over twenty years and delaying replacement until after the end of the test year. Exclusion of either of these trucks from rate base will deny the Company proper recovery for equipment used and useful in service to its consumers and will require the filing of another rate case, at much cost to the Company and its ratepayers, sooner. In addition, the Department's standard is intended to allow significant changes to rate base. The replacement of one/third of its total transportation "fleet" is certainly significant. Given the age of these vehicles, failure to replace them would impede Blackstone's ability to install pipe and perform maintenance. If Blackstone had purchased these trucks during the test year, presumably there would be no question but that they were a necessary investment. One of the Department's rationales for excluding ordinary plant additions because offsetting retirements are not easily identified. With regard to transportation equipment, the offsetting retirements have been clearly identified. The Company has in fact retired two vehicles, which had no remaining book value. The Attorney General suggests there should be post-test year revenue associated with the transportation equipment. This suggestion is inappropriate for this type of plant. Transportation equipment is not a main extension where there are new customers and new revenues associated with the project. The two trucks add no revenue to the Company.

The Company will not press the two other smaller post-test year rate base addition requests.

2. Cash Working Capital for Gas Costs

The Company indicated its preference to include cash working capital for gas in base rates as this allows the Company to more accurately allocate the costs of this expense to the various classes. However, the Company will not object to the inclusion of a working capital allowance for gas in its CGA. The September 2001 CGA filing by the Company does not include a provision for gas work capital and thus a revised CGA will have to be filed at the conclusion of this case if the Department determines that a gas cash working capital allowance should be included in the CGA.

D. Expenses

1. Bad Debt Expenses

The Company proposed an uncollectible expense derived from the most recent two years experience rather than a three year average to better reflect the steeply increasing bad debts. This resulted in a bad expense ratio of 1.00% of the Company's normalized revenue. RR-AG-6.

While the normal Department precedent is to use three years to create a bad debt expense ratio, RR-AG-6 explains the basis for deviation from this standard to derive a representative bad debt ratio for the Company.

As noted by the Attorney General in his Brief at p. 12, the booked uncollectible expense for the Company has varied over the past six years. For three years the bad debt expense was less than $7,700 and in three years it was over $12,100. The average bad debt expense over this 6 year period is $9,698. The average total revenues for the six year period as shown in the Annual Returns to the Department is $953,133. Exh. AG-1-2 (Annual Returns to Department, Account 400, p. 43.) The average bad debt expense over the six year period is 1.02%. Thus, the bad-debt expense ratio figure used by the Company is much more representative of bad debt expense than the arbitrarily selecting the last three years which includes two years of abnormally low write-offs.

2. The Company's Wage Level is Reasonable

The Company because of its size and customer base has relatively few employees. AG-1-3. The level of gas company employee payroll has increased from $190,795 in 1995 to $241,034 in the test year. Exh. DTE-1-15. The total increase in payroll over this five year period is $50,239.50. Id. This is a 26.3% increase in payroll expense or an average of 5.26% per year. Reference to percentage increases for salary and wages alone in a small company like Blackstone should not be controlling.

During the test year the Company granted a significant percentage increase in order to retain a qualified person to supervise pipeline safety and related matters. Tr. 2-02-204. This required a 36% increase in the salary of the distribution supervisor bringing this skilled employee to the level of $65,798. Exh. RR-DTE-8.

Blackstone checked with other gas utilities in New England and obtained two data points which indicate that even with the major adjustment in the salary of the distribution supervisor his salary is still approximately $9,500 to $13,600 below the midpoint of the range of two other local distribution companies.

Blackstone does not claim Exh. RR-DTE-8 is a full blown wage survey, which would cost thousands of dollars, but rather is a reasonable check on the salary level of reasonably comparable positions in other companies. To require any further proof for the Company is not cost-effective for the Company or its ratepayers.[2]

In addition, the Company checked salaries of managers of Wakefield Municipal Gas and Light Department and Westfield Gas and Electric Department and found that their salaries were $94,350 and $122,819 respectively. Exh. DTE-1-15. In comparison, the salary for the president of Blackstone is $76,113. Id. Again, this is not a scientific survey, but it does demonstrate the reasonableness of the salary of the president of the company.

With the exception of the president and the distribution supervisor there is only one other Company employee who, after their 2000 increase, has a salary that exceeds $32,000 per year. See Exh. DTE-1-14 and Exh. AG-2-7. These wage levels are reasonable and should be approved by the Department. Accordingly, the wage increases granted during the test year and the normalizing adjustment to the total wage levels of the employees of the Company are reasonable and comply with the Department's non-union wage adjustment standard as outlined in Boston Gas Company, D.P.U. 96-50 (Phase I) pp. 42-43, as there is an express commitment by management to grant the increases, as they have already been granted; there is no union so no requirement to have a correlation between union and non-union increases; and the total wage level is reasonable.

[2] Blackstone did try to obtain a copy of a confidential wage survey filed by another larger gas utility. Blackstone was unable to obtain a copy of such survey, which is in the possession of both the Department and the Attorney General.

The wage normalizing adjustment made by the Company did not reflect expected future increases in wage levels. This adjustment only reflected the effect of wage increases made almost entirely in the first 20 weeks of 2000. Exh. AG-2-7. Thus, this adjustment simply normalized wages to the average level of wages at the mid-point of the test year. Blackstone agrees that the wage increase of $1,520 made after the 38th week of the year should be removed from this adjustment.

3. Liability Insurance Should Not Be Allocated to the Company's Affiliate

The Company proposes to increase its test-year cost of service by $5,886. Exh. B-4, Schedule 3. This represents the increase in liability insurance expense for the policy year commencing April 5, 2001 to April 5, 2002. Exh. AG-2-11.

The Company has allocated none of the cost for liability insurance to its Sales and Service Affiliate. The Company rationale for not allocating any cost of its liability insurance to the affiliate is as follows: when the gas company attempted to obtain liability insurance for the gas company on a stand-alone basis the minimum cost was in excess of the total current liability insurance expense included in the cost of service. Exh. RR-DTE-2. It was only because of the availability of liability insurance through a carrier that insures propane companies that the gas company was able to obtain liability insurance at as low a cost as set forth in the cost of service study including the pro forma adjustment. Thus, the value of the liability insurance to the gas company is greater than its cost and no charge should be allocated to the propane affiliate.

4. Allocation of Officers' Salaries and Benefits

There are two officers of the Company that are also employees, Mr. James Wojcik, the President and Mrs. Grace Wojcik, the Clerk. During the proceedings no party questioned the allocation of the salaries or benefits of these two employees. In his Brief the Attorney General contends that the salary and benefits of these two employee-officers should be allocated to the unregulated Sales and Service Division based on a revenue allocator of 32.9 percent. There is no reasonable basis to utilize a revenue allocator to allocate the salary and benefits of these officers.

Since this issue was not raised during the proceedings, the Company is filing a Motion to Supplement the Record and an Affidavit of James Wojcik to provide the Department with the facts surrounding the time spent by each officer on matters related to the regulated and unregulated divisions. Without the facts in this affidavit there is no basis to allocate any amount of the salary or benefits of the officers to the unregulated division.

The Affidavit indicates that Mrs. Wojcik spends no time on the business of the unregulated division and thus none of her salary or benefits should be allocated to the unregulated division. Mr. Wojcik, the President, spends more than 40 hours per week on average on the regulated gas company matters and 2 hours per week on average on propane procurement for the unregulated division. Thus, on a time spent basis no more than 5% of the salary and benefits of Mr. Wojcik should be allocated to the unregulated division. However, Mr. Wojcik receives additional compensation of $150 per week from the unregulated division. Thus, none of his salary or benefits should be allocated to the unregulated division. As noted above, at a salary of $76,113 Mr. Wojcik is paid less than a manager of at least two municipal electric and gas departments. Any allocation of this salary would further reduce the salary of Mr. Wojcik for the regulated gas division in an unreasonable manner.

5. Inflation Adjustment

The Company agrees that it should remove the (1) bad debt expense, (2) the unbundling expense, and (3) liability expense from its inflation adjustment. The Company does not agree that the (1) rent and lease expense, or (2) wages should be removed from the inflation adjustment. Rent and lease expense is not a fixed expense that does not increase as suggested by the Attorney General. AG Brief, p.18. The rent figure is very low and the Company anticipates a significant increase starting January 1, 2001.

The Attorney General misunderstands the Department policy regarding inflation adjustment and how the Company has treated wage increases. The inflation adjustment should be made to expenses which are not treated separately elsewhere, usually because they are too small. For larger utilities, labor is usually adjusted separately on the basis of union contracts, and it would be double counting to adjust them twice. Blackstone did not make a separate projection of post-test year increases in wages. Its only adjustment was to normalize test year labor costs so they reflected middle of test year wage levels. If Blackstone had done as larger companies usually do, it would have asked for a separate but much larger adjustment to reflect its average past level of wage increases of 5% per year. If wages were simply pulled out of the inflation adjustment made by Blackstone, the Company would receive no compensation for any post-test year increase.

6. Income Tax Calculation

During the proceedings the parties questioned the income tax calculation submitted by the Company in its cost of service with regard to the deductibility of state income taxes from federal income taxes and whether the effective tax rates utilized by the Company properly reflected the pro forma tax rate applicable to the Company. The Company demonstrated that its methodology and the methodology suggested by the Attorney General were the same. Exh. Blackstone –2.

In his brief, AG- Brief, pp. 19-20, the Attorney General raised for the first time another issue relative to the income tax calculation—the use of pro forma interest expense based on the rate base methodology rather than the actual test year interest expense used by the Company. After review of the issue the Company accepts the adjustment proposed by the Attorney General to use the pro forma interest expense based on the rate base methodology by multiplying the rate base times the debt component of the overall cost of capital. This issue could have been resolved much earlier in the proceeding if the Attorney General had brought the issue to the attention of the Company.

E. Rate Design

1. Allocation of Rate Increase

The Company filed an allocated cost of service study which indicated the following revenue deficiency by class from Exhibit Blackstone-4, Exh. 2, Schedule 1.

Residential Heating	$ 71,730	9.6%
Residential Non-heating	5,347	13.0%
Commercial	60,069	16.4%
School Rate	25,555	56.9%
Total Company	$162,709	13.67%

Originally the required revenue increase was 18.4% and the Company proposed to increase each class by the average increase of 18.4%. The Attorney General has objected to the rate design proposed by the Company in so far as it does not equalize the rate of return for the School Rate. AG Brief, pp. 20-23.

The Company has provided evidence that the School Rate is an outgrowth of two special contracts filed with and approved by the Department for the Company to serve the Kennedy Maloney School in Blackstone. Exhs. RR-AG-13 and RR-AG-13 Supplemental.

In this proceeding the Company is proposing to increase the rate to the School 18.4% even if the Department approves a rate increase less than originally requested. This will move the School Rate closer to a fully allocated cost of service. Any further increase in the School Rate at this time would violate continuity considerations and be unfair to the School. The Attorney General suggests that the Company should forego any revenue deficiency resulting from the School Rate being set at less than cost of service. AG Brief, p.22. This solution is unfair and not acceptable to the Company.

First, an allocated cost of service study is only a reasonable approximation of cost allocation and is not the only factor followed by the Department in allocation, revenue deficiency. Second, the Department has recognized rate continuity and other factors in its decisions on the allocation of a revenue deficiency. Here the Department must consider other factors. For instance, the School was added as an incremental customer to contribute some revenues to the Company and its customers and that the School was originally an oil customer and would not have switched to gas under a fully allocated cost contract. Exh. RR-AG-13. The revenues received from this customer recovered the costs directly associated with adding this customer within one year, and the existence of this customer and its revenues reduced the rates requested by the Company in its 1995 rate case. Id. The Department approved this rationale and should not now penalize the Company or the customer. The department never put the

Company on notice that this customer must be served on a fully allocated cost basis. If the Department requires a fully allocated cost approach to the School, the School could well return to oil and all revenues provided to offset the cost of service for other customers would be lost. The Department should view this School Rate as an incremental customer or rate and allocate its contributions to the benefits of all customer classes. It should not penalize either the Company or the customer. The proposed School Rate recovers all gas costs as contained in the CGA. Thus all additional revenues are incremental for the benefit of other customers.

2. Low-Income Residential Rates

The Company has proposed a low-income rate for residential heating and non-heating customers which would provide a 25% base rate discount from the proposed normal residential rates. Exh. Blackstone-1, pp. 15-17. Because the Company has no accurate basis to estimate the penetration level of the discount rates, it estimated that 5% of the residential heating class and none of the nonheating class would select the discounted rates. This estimate was based on the experience of North Attleboro Gas Company with low-income rates. Id. Adoption of the low-income rates will result in the reallocation of approximately $4,000 to other customers based on the estimated penetration level.

Since the low-income rates are new for the Company, they expose Blackstone to considerable revenue uncertainty. If the enrollment on the rates is at a higher rate than North Attleboro has experienced, Blackstone could undercollect its revenue requirement by a significant amount. Blackstone requests that should the enrollment and revenue shortfall from the subsidized rate be greater than projected, it be allowed to defer any undercollection and recover the shortfall through the LDAC or in the next base rate case.

III. CONCLUSION

Wherefore the Company submits that it should be allowed to increase rates by the amount set forth on Exh. Blacksone-4 as modified by the Company in this brief.

Respectfully submitted,

BLACKSTONE GAS COMPANY
by its attorneys

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